

Revised
Texas
Franchise
Tax



Combined Reporting

Section 171.1014 / Rule 3.590

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Combined Reporting - Mandatory

Texas Tax Code 171.1014

- (a) Taxable entities that are part of an affiliated group engaged in a unitary business shall file a combined group report in lieu of individual reports based on the combined group's business.
- (b) The combined group is a single taxable entity for purposes of the application of the tax imposed under this chapter.

Combined Reporting - Definitions

Combined group--Taxable entities that are part of an affiliated group engaged in a unitary business and that are required to file a combined group report under Tax Code, sec. 171.1014.

Affiliated group--Entities in which a controlling interest is owned by a common owner, either corporate or noncorporate, or by one or more of the member entities.

Controlling interest-- means more than 50%, owned directly or indirectly, of the stock of a corporation; of the membership interest of a limited liability company; or an interest in a partnership, association, trust, or other entity. (Attribution Rule - husband and wife are deemed to be one owner; no other family attribution.)

Combined Reporting - Definitions

Unitary business--A single economic enterprise that is made up of separate parts of a single entity or of a commonly controlled group of entities that are sufficiently interdependent, integrated, and interrelated through their activities so as to provide a synergy and mutual benefit that produces a sharing or exchange of value among them and a significant flow of value to the separate parts.

In determining whether a unitary business exists, the comptroller shall consider any relevant factor, including whether:

- activities of the members are in the same general line of business;
- activities of the members are steps in a vertically structured enterprise or process; or
- members are functionally integrated through the exercise of strong centralized management.

Combined Reporting - Definitions

Reporting entity--The combined group's choice of an entity that is:

- the parent entity, if it is part of the combined group, or
- the entity that:
 - is included within the combined group;
 - is subject to Texas' taxing jurisdiction; and
 - has the greatest Texas business activity during the first period upon which the first combined group report is based, as measured by the Texas receipts after eliminations for that period.

Combined Reporting - Members

All affiliated and unitary taxable entities even if those entities do not have nexus in Texas.

Includes pass-through entities:
partnerships, limited liability companies taxed as partnerships under federal law, limited liability companies that are disregarded under federal law, S corporations, and trusts.

Combined Reporting – Excluded Entities

80/20 Affiliates--if an affiliate has 80% of its property or payroll outside of the US.*

Exempt Entities--entities that have an exemption from the franchise tax under Subchapter B of Chapter 171.

Insurance Companies--that pay gross premiums tax.

Passive Entities--not included in the combined group; however, the pro rata share of net income from a passive entity shall be included in total revenue to the extent it was not generated by the margin of another taxable entity.

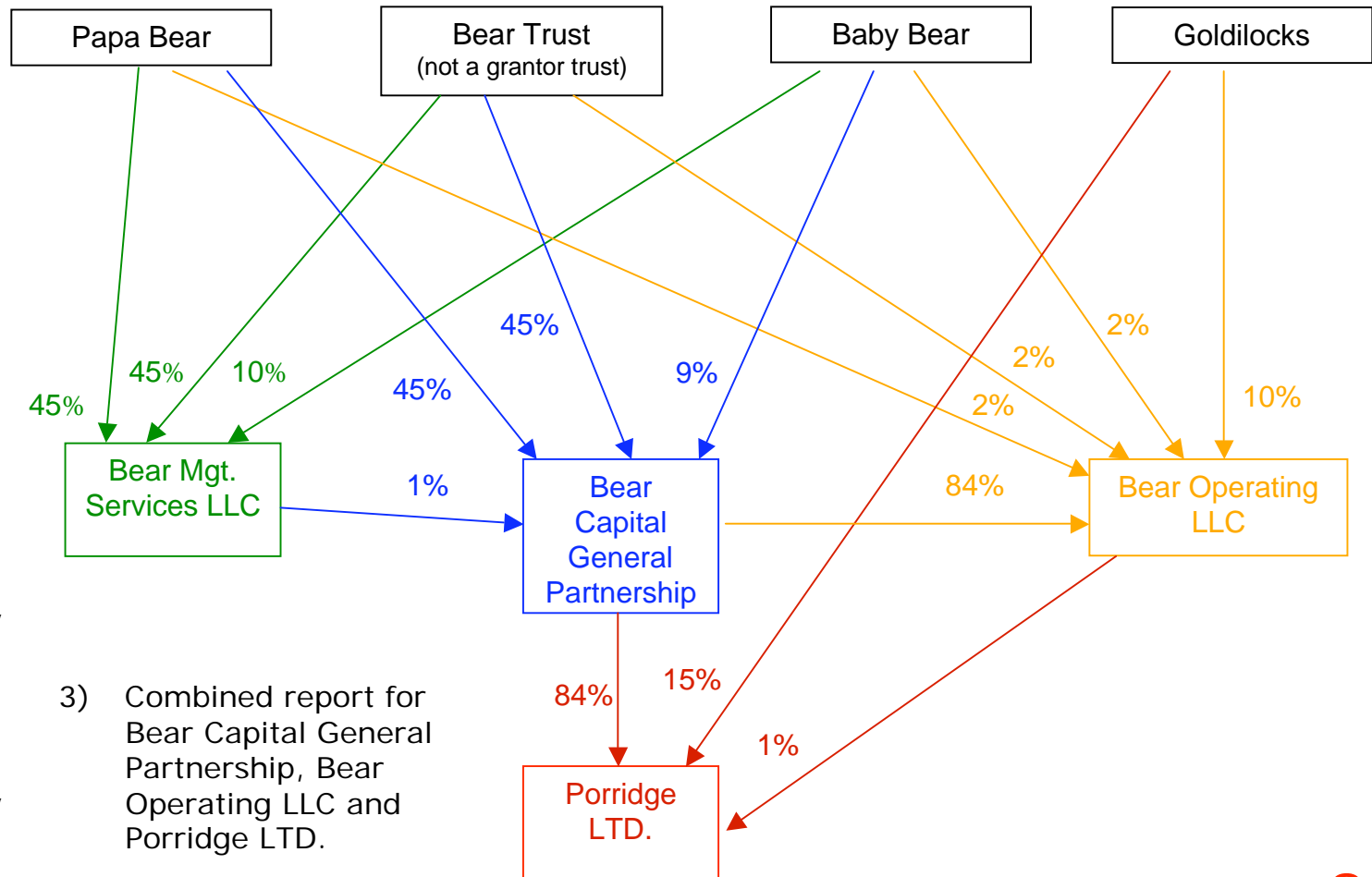
* 80/20 affiliates with nexus in Texas are required to file a separate franchise tax report.

Combined Reporting – Example

Result:

Based on these facts and presuming that neither of the partnerships or the trust qualified as passive entities, three franchise tax reports would be filed.

- 1) Bear Trust – separate entity report
- 2) Bear Mgt Services LLC – separate entity report
- 3) Combined report for Bear Capital General Partnership, Bear Operating LLC and Porridge LTD.



Combined Reporting – Calculation Options

The reporting entity must “elect” a method of reporting for the entire group:

- Margin - 70% of Total Revenue
- Margin - Total Revenue minus COGS
- Margin - Total Revenue minus Compensation
- E-Z Computation

Combined Reporting – Total Revenue

A combined group shall determine its total revenue by:

- determining the total revenue of each of its members as if the member were an individual taxable entity;
- adding together the total revenues of each of the members; and
- subtracting, to the extent included, items of total revenue received from a member of the combined group.

Combined Reporting – Cost of Goods Sold

A combined group shall determine its COGS by:

- determining the COGS of each of its members as if the member were an individual taxable entity (only if the member sells real or tangible personal property in the ordinary course of business) ;
- adding together the COGS of each of the members; and
- subtracting, any COGS amounts paid from one member of the group to another member of the group, but only to the extent the corresponding item of total revenue was subtracted.

Note: The election to capitalize or expense allowable costs in computing COGS must be the same for all members of the combined group.

Combined Reporting – Compensation

The combined group may not subtract in relation to a person, more than \$300,000 or the amount determined under Tax Code, sec. 171.006, per 12-month period on which margin is based. A combined group that elects to subtract compensation shall determine that amount by:

- determining the compensation of each of its members as if the member were an individual taxable entity; and
- adding together the compensation of each of the members.

Combined Reporting – Apportionment

Texas Gross Receipts / Everywhere Gross Receipts

Texas gross receipts includes receipts from business done in this state by taxable entities with nexus in Texas.*

Everywhere gross receipts includes receipts from business done everywhere by all members of the group.

* Exception – drop shipments made by a member of the group from a Texas location to a Texas purchaser will be included in Texas receipts even if the seller is a no-nexus member of the group.

See rule 3.591, Margin: Apportionment, for more information.

Combined Reporting – Accounting Period

The accounting period of the group shall be:

- The accounting period used for federal tax reporting if two or more members of the combined group file a consolidated federal return.
- In all other instances, the accounting period is the federal taxable period of the reporting entity.

Note: If the federal tax period of a member differs from the federal tax period of the group, the reporting entity will determine the portion of that member's revenue, cogs, compensation, etc. to be included by preparing a separate income statement using information on the federal report for the months included in the group's accounting period.

Combined Reporting – Accounting Period

Facts:

- ❑ Corporation A is a separate entity from 1/1/07 through 6/30/07.
- ❑ On July 1, 2007 Corp A was acquired by Corp X combined group and is owned by them until 9/30/07. X has a 3/31/07 accounting year end.
- ❑ On October 1, 2007 A is sold by X to Z.
- ❑ Group Z has a 12/31 AYE.
- ❑ Corp A had \$250,000 in total revenue for the period of 1/1/07 – 6/30/07.

Result:

- ❑ Corp A will file on its own for the period 1/1/07 through 6/30/07. It does not qualify for a No Tax Due report based on total revenue. It's annualized Total Revenue is \$500,000 which is greater than the \$300,000 threshold.
- ❑ Corp X group will file a combined report on May 15, 2008 based on the period 4/1/06 through 3/31/07. It will NOT include Corp A in the 2008 report because A was not part of the group during the period upon which the tax is based. It will include Corp A in its 2009 annual report for the period 7/1/07 through 9/30/07.
- ❑ Corp Z group will file a combined report on May 15, 2008 based on the period 01/01/07 through 12/31/07 and will include Corp A's data for the period 10/01/07 through 12/31/07.

Combined Reporting – 0.5% Tax Rate

The revenue from each retail and wholesale trade activity of each of the members of the group shall be aggregated for purposes of determining whether the group is engaged in retail or wholesale trade (after eliminations).

Taxable Entities primarily engaged in retail or wholesale trades will qualify to use the 0.5% tax rate.

A taxable entity is primarily engaged in retail or wholesale trade only if:

- (1) the total revenue from its activities in retail or wholesale trade is greater than the total revenue from its activities in trades other than the retail and wholesale trades;
- (2) less than 50 percent of the total revenue from activities in retail or wholesale trade comes from the sale of products it produces or products produced by an entity that is part of an affiliated group to which the taxable entity also belongs (this does not apply to Eating & Drinking Places described in Major Group 58 of Division G); and
- (3) the taxable entity does not provide retail or wholesale utilities, including telecommunications services, electricity or gas.

Combined Reporting – Miscellaneous

No Tax Due – a combined group is not eligible to file a no tax due report.

E-Z Computation – if the combined group has annualized total revenue of \$10 million or less (after eliminations) it may elect to pay its franchise tax using the E-Z method. No tax credits may be taken if E-Z is elected. Business loss credits for that period are lost – they may not be carried to future reports.

Annualized Total Revenue – for a combined group is based on total revenue after eliminations.

Discounts – based on annualize total revenue of the combined group.

(80% if TR > \$300,000 & < \$400,000; 60% if TR \geq \$400,000 & < \$500,000; 40% if TR \geq \$500,000 & < \$700,000; 20% if TR \geq \$700,000 & < \$900,000)

Combined Reporting –Credits

Business Loss Credit - - Members of a combined group MUST preserve their right to take the credit on a separate company basis. The reporting entity will add the preserved amounts of all members together, multiply by 2.25% (for report years 2008 – 2017; 7.75% for 2018 – 2027) then multiply by 4.5% to calculate the credit for the report period. Credit for a member is lost if the member leaves the group. Member must be in group at year end.

Economic Development Credits - - The reporting entity may take any installments or carryovers of economic development credits previously created by members of the group.

Contact Us!

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Tax Questions?

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